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No. 05-1126

IN THE

Supreme Court of the United States

BELL ATLANTIC CORPORATION, *ET AL.*,
Petitioners,
v.
WILLIAM TWOMBLY, *ET AL.*, INDIVIDUALLY AND ON BEHALF OF ALL OTHERS SIMILARLY SITUATED,
Respondents.

On Writ of Certiorari to the United States Court of Appeals for the Second Circuit

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QUESTION PRESENTED

Whether a complaint states a claim under Section 1 of the Sherman Act, 15 U.S.C. § 1, if it alleges that the defendants engaged in parallel conduct and adds a bald assertion that the defendants were participants in a "conspiracy," without any allegations that, if later proved true, would establish the existence of a conspiracy under the applicable legal standard.

LIST OF PARTIES TO THE PROCEEDINGS

Petitioners Bell Atlantic Corporation, BellSouth Corporation, Qwest Communications International Inc., SBC Communications Inc. (now known as AT&T Inc.), and Verizon Communications Inc. (successor-in-interest to Bell Atlantic Corporation) were defendants in the district court and appellees in the court of appeals.

Respondents William Twombly and Lawrence Marcus, both individually and on behalf of all others similarly situated, were plaintiffs in the district court and appellants in the court of appeals.

CORPORATE DISCLOSURE STATEMENTS

Pursuant to Rule 29.6 of the Rules of this Court, petitioners Bell Atlantic Corporation, BellSouth Corporation, Qwest Communications International Inc., SBC Communications Inc. (now known as AT&T Inc.), and Verizon Communications Inc. (successor-in-interest to Bell Atlantic Corporation) state the following:

Bell Atlantic Corporation. On June 30, 2000, GTE Corporation and Bell Atlantic Corporation merged, and Bell Atlantic Corporation subsequently changed its name to Verizon Communications Inc., its successor-in-interest. Verizon Communications Inc. has no parent company, and no publicly held company owns 10% or more of its stock.

BellSouth Corporation. BellSouth Corporation has no parent company, and no publicly held company owns 10% or more of its stock.

Qwest Communications International Inc. Qwest Communications International Inc. has no parent company. Qwest's securities are publicly traded. As of August 22, 2006, the following publicly held corporations had reported ownership of 10% or more of the publicly issued securities of Qwest Communications International Inc.: Legg Mason, Inc. (through various wholly owned subsidiaries).

SBC Communications Inc. On November 18, 2005, SBC Communications Inc. merged with AT&T Corp. and changed its name to AT&T Inc. AT&T Inc. has no parent company, and no publicly held company owns 10% or more of its stock.

Verizon Communications Inc. Verizon Communications Inc. is the successor-in-interest to Bell Atlantic Corporation. Verizon Communications Inc. has no parent company, and no publicly held company owns 10% or more of its stock.

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OPINIONS BELOW

The court of appeals' opinion (Pet. App. 1a-34a) is reported at 425 F.3d 99. The district court's opinion (Pet. App. 35a-58a) is reported at 313 F. Supp. 2d 174.

JURISDICTION

The court of appeals entered its judgment on October 3, 2005. A timely petition for rehearing was denied on January 3, 2006. Pet. App. 59a-60a. The petition for a writ of certiorari was filed on March 6, 2006, and was granted on June 26, 2006 (126 S. Ct. 2965). The jurisdiction of this Court rests on 28 U.S.C. § 1254(1).

STATUTORY PROVISIONS INVOLVED

Section 1 of the Sherman Act, 15 U.S.C. § 1, is set forth at Pet. App. 61a.

STATEMENT OF THE CASE

Plaintiffs below are representatives of a purported class consisting of all users of telephone and Internet service in the continental United States over the past decade. Plaintiffs alleged that incumbent telephone companies, acting in parallel: (1) resisted new entrants' efforts to enter their respective markets and (2) failed to compete in each others' territories as new entrants. To these allegations of purely parallel conduct, plaintiffs added a bald allegation that defendants were engaged in a conspiracy – though they did not say when (sometime in the last decade); they did not say where (somewhere in the continental United States); and they did not say who (the four defendants have nine major corporate predecessors and hundreds of thousands of employees). Plaintiffs implicitly conceded below that they lacked any basis to make such *direct* factual allegations of conspiracy. Instead, plaintiffs relied entirely on the *inference* of conspiracy that they claimed should be drawn from the alleged parallel conduct.

The district court (Lynch, J.) held that these allegations failed to state a claim under Section 1 of the Sherman Act. The court held that when a complaint seeks to draw an

inference of agreement from allegations of otherwise lawful parallel conduct

> the basic requirement that plaintiffs must fulfill is to allege facts that, given the nature of the market, render the defendants' parallel conduct, and the resultant state of the market, suspicious enough to suggest that defendants are acting pursuant to a mutual agreement rather than their own individual self-interest.

Pet. App. 46a. The district court went on to hold that the complaint failed to meet that standard because the parallel conduct alleged by plaintiffs was perfectly explicable in terms of independent self-interest and did not support an inference of conspiracy under this Court's precedents.

The court of appeals reversed. It rejected the district court's standard and held instead that

> to rule that allegations of parallel anticompetitive conduct fail to support a plausible conspiracy claim, a court would have to conclude that there is *no set of facts* that would permit a plaintiff to demonstrate that the particular parallelism asserted was the product of collusion rather than coincidence.

Id. at 25a (emphasis added). Under the Second Circuit's standard, a complaint alleging otherwise innocuous parallel conduct can survive a motion to dismiss based merely on the *possibility* that facts not alleged might yet be found that would support the claim for relief. That decision, wrong as a matter of pleading law and harmful as a matter of antitrust policy, should be reversed.

A. Background

1. In 1982, the AT&T divestiture decree created seven Regional Bell Operating Companies ("Bell companies") and assigned each of them to a different portion of the country. *See United States v. AT&T Co.*, 552 F. Supp. 131 (D.D.C. 1982), *aff'd mem. sub nom. Maryland v. United States*, 460 U.S. 1001 (1983). These seven Bell companies – predeces-

sors of the four defendants – provided local telephone service pursuant to state-authorized exclusive franchise arrangements but were barred from offering long-distance service. *See AT&T Corp. v. Iowa Utils. Bd.*, 525 U.S. 366, 413-14 (1999) (Breyer, J., concurring in part and dissenting in part).

The Telecommunications Act of 1996 (the "1996 Act") dramatically changed this regime. It eliminated the state-authorized exclusive franchises that had prevented entry in most local telephone markets, and it enacted a series of affirmative obligations, binding on the Bell companies and other incumbent telephone companies, intended to jump-start competitive entry. In return for opening their local markets to competition, Bell companies were promised the opportunity – once they demonstrated full compliance with their market-opening obligations – to enter the long-distance business on a state-by-state basis. *See generally* 47 U.S.C. § 271. Between 1999 and 2003, after spending billions of dollars on regulatory compliance efforts, and having their market-opening efforts exhaustively scrutinized by the Department of Justice and by federal and state regulatory authorities, all the Bell companies earned approval to offer long-distance service in their respective states.

2. Among the obligations created by the 1996 Act was the requirement that incumbents "unbundle" – that is, share with new entrants at low, cost-based rates – certain elements of their local networks. *See Verizon Communications Inc. v. Law Offices of Curtis V. Trinko, LLP*, 540 U.S. 398, 405-06 (2004). Section 251(d)(2) directed the Federal Communications Commission ("FCC") to determine "what network elements should be made available" by incumbents based on whether lack of access to such elements would "impair the ability" of new entrants to provide competing telephone service. 47 U.S.C. § 251(d)(2). In its *Local Competition Order*, 11 FCC Rcd 15499, ¶¶ 367-451 (1996), the FCC directed the incumbents to make available *all* of the facilities required to provide basic local telephone service. As a result, new entrants could rely on a complete "platform" of "unbundled

network elements" (known as the "UNE-platform" or "UNE-P") at cost-based rates without investing in any facilities of their own.

The FCC's UNE-P regime did not survive judicial review. First, this Court vacated the FCC's "blanket" unbundling rules in *Iowa Utilities Board*. *See* 525 U.S. at 387-92. After the FCC re-adopted those rules virtually unchanged in its *UNE Remand Order*, 15 FCC Rcd 3696 (1999), the D.C. Circuit vacated them. *See USTA v. FCC*, 290 F.3d 415, 422 (D.C. Cir. 2002) ("*USTA I*"), *cert. denied*, 538 U.S. 940 (2003). Despite these two judicial vacaturs, the FCC, in its 2003 *Triennial Review Order*, 18 FCC Rcd 16978 (2003), issued new unbundling rules that again sought to preserve blanket unbundling in most circumstances, leading to a second vacatur by the D.C. Circuit. *See USTA v. FCC*, 359 F.3d 554, 576 (D.C. Cir.) ("*USTA II*"), *cert. denied*, 543 U.S. 925 (2004). Finally, in the wake of *USTA II*, the FCC adopted rules that phased out the UNE-P, *see Triennial Review Remand Order*, 20 FCC Rcd 2533 (2005), a decision that the D.C. Circuit recently upheld, *see Covad Communications Co. v. FCC*, 450 F.3d 528 (2006).

Throughout this period, the incumbents (also called "incumbent local exchange carriers" or "ILECs") generally continued, under pressure from regulators, to make the UNE-P available to new entrants without interruption, until the FCC finally ruled that such access was no longer required. Despite extreme uncertainty as to whether the UNE-P would remain available, many new entrants – companies known as "competitive local exchange carriers" or "CLECs" – widely relied on it. Indeed, as a result of "highly attractive" cost-based rates, *USTA I*, 290 F.3d at 424, the UNE-P became almost the exclusive focus of CLEC efforts to reach local residential and small business (*i.e.*, "mass market") customers: by mid-2004, dozens of CLECs were serving, in total, more than 17 million customers using the UNE-P. With the elimination of the UNE-P, however, the number of mass-market customers served by CLECs declined rapidly, even though

ILECs made replacement arrangements available at market-based prices. *See* Industry Analysis & Technology Division, Wireline Competition Bureau, FCC, *Local Telephone Competition: Status as of December 31, 2005*, at Table 4 (July 2006).

B. The Complaint

Almost from the start, the 1996 Act spawned not only "interminable" regulatory litigation at the state and federal level, *Trinko*, 540 U.S. at 414, but also a parallel track of antitrust litigation.

Most of these cases made essentially the same claim: that ILECs' alleged failure to share their networks adequately had frustrated CLEC entry and constituted "exclusionary conduct" prohibited by Section 2 of the Sherman Act. In 2002, the Second Circuit, reversing a decision of the district court, ruled that such allegations stated a claim. *See Law Offices of Curtis V. Trinko, LLP v. Bell Atlantic Corp.*, 309 F.3d 71 (2d Cir. 2002), *rev'd*, 540 U.S. 398 (2004). Following that ruling, William Twombly sued SBC in the District of Connecticut, on behalf of a purported class, under Section 2. He claimed that 12 categories of conduct, all related to insufficient sharing by SBC, constituted anticompetitive conduct designed "to restrain, stifle and delay any meaningful competition for local telephone and/or high-speed internet services." Consol. Am. Class Action Compl. ¶ 30, *In re SBC Communications, Inc. Antitrust Litig.*, No. 3:02CV1617 (DJS) (D. Conn. filed Feb. 19, 2003). (Twombly was not alone: class action plaintiffs filed multiple lawsuits against SBC and Verizon in the Second Circuit.) After this Court reversed the Second Circuit in *Trinko*, holding that the claims of insufficient sharing were not actionable under Section 2, Twombly abandoned his monopolization complaint.

But the claims continued in another form. Twombly, later joined by a second purported class representative, brought this separate class action complaint in the Southern District of New York under Section 1. In their consolidated

complaint, plaintiffs alleged that "Defendants . . . have engaged and continue to engage in unanimity of action by committing one or more of the following wrongful acts in furtherance of a common anticompetitive objective to prevent competition . . . in their respective local telephone and/or high speed internet services markets"; the complaint then listed precisely the same 12 categories of conduct that provided the basis for Twombly's earlier complaint under Section 2. JA 24-26 (Am. Compl. ¶ 47). The complaint added one more allegation: that defendants "have refrained from engaging in meaningful head-to-head competition in each other's markets." JA 21 (¶ 39).

Although plaintiffs alleged that "Defendants and their co-conspirators engaged in a contract, combination or conspiracy," JA 30 (¶ 64), the complaint made clear that the sole basis for the allegation was the observed marketplace conduct of defendants (and one newspaper quote attributed to one of the defendant's executives). Plaintiffs alleged no facts directly indicating any agreement among defendants. The complaint failed to allege when the agreement was reached, "the exact dates being unknown to Plaintiffs." *Id.* The complaint failed to identify which of the corporate predecessors of the four defendants participated in the conspiracy. It equally failed to identify any of the "other persons, firms, corporations and associations" that also allegedly participated in the conspiracy. JA 14 (¶ 16). And, although the complaint alleged that defendants "communicate amongst themselves through a myriad of organizations," JA 23 (¶ 46), it neither suggested that such communications are suspicious in this industry (where, for example, network interconnection and standard-setting require joint activities) nor identified a single occasion on which any relevant agreement was reached, the mechanism for enforcing any such agreement, or any individual parties involved in making, enforcing, or carrying out any such agreement.

Instead, plaintiffs "allege[d] *upon information and belief*," "[i]n the absence of any meaningful competition between the

[defendants] in one another's markets, and in light of the parallel course of conduct that each engaged in to prevent competition from [new entrants]," that "Defendants have entered into a contract, combination or conspiracy." JA 27 (¶ 51) (emphasis added).

Plaintiffs also included two types of allegations intended to bolster their conjecture. First, with regard to the alleged agreement to resist sharing their network facilities, the complaint alleged that, "[h]ad any one of the Defendants not sought to prevent CLECs . . . from competing effectively . . . , the resulting greater competitive inroads into that Defendant's territory would have revealed the degree to which competitive entry by CLECs would have been successful in the other territories in the absence of such conduct" and "would have enhanced the likelihood that such a CLEC might present a competitive threat in other Defendants' territories as well." JA 26-27 (¶ 50).

Second, with regard to the alleged agreement not to compete meaningfully as CLECs, the complaint alleged that the "structure of the market . . . is such as to make a market allocation agreement feasible" in that "[e]laborate communications . . . would not have been necessary in order to enable Defendants to agree to allocate territories" and "[i]f one of the Defendants had broken ranks and commenced competition in another's territory the others would quickly have discovered that fact." JA 26 (¶¶ 48, 49). Plaintiffs further argued that each defendant's failure to compete significantly even where their respective traditional local service territories abut or in some cases surround those of the other defendants "would be anomalous in the absence of an agreement." JA 21 (¶ 40). The complaint alleged that, in competing for business in such nearby areas, each defendant would have "substantial competitive advantages," *id.* (¶ 41), though the complaint did not identify them – and did not allege that the asserted advantages made entry into nearby areas a better use of any defendant's resources than other business opportunities or needs. Moreover, plaintiffs alleged, an executive of one of

the defendants had commented that competing as a CLEC in the territory of one of the other defendants "might be a good way to turn a quick dollar but that doesn't make it right," JA 22 (¶ 42), 41, ignoring the same executive's statement, in the same article, that such entry is not a "sustainable economic model," *see* JA 42.

C. The District Court's Decision

The district court granted defendants' motion to dismiss for failure to state a claim. Judge Lynch began by noting that, "absent an agreement among competitors to restrain trade, anti-competitive behavior does not violate § 1." Pet. App. 40a. Accordingly, to establish their entitlement to relief under Federal Rule of Civil Procedure 8(a), plaintiffs must allege facts that, drawing all inferences in plaintiffs' favor, show the existence of such an agreement.

Noting the absence of direct factual allegations to support the existence of any agreement, Judge Lynch began his analysis by observing that "simply stating that defendants engaged in parallel conduct, and that this parallelism must have been due to an agreement, would be equivalent to a conclusory, 'bare bones' allegation of conspiracy" and "insufficient to withstand a motion to dismiss." *Id.* at 42a. "In the context of parallel conduct claims, the basic requirement that plaintiffs must fulfill is to allege facts that, given the nature of the market, render the defendants' parallel conduct, and the resultant state of the market, suspicious enough to suggest that defendants are acting pursuant to a mutual agreement rather than their own individual self-interest." *Id.* at 46a. Such facts could "include evidence that the parallel behavior would have been against individual defendants' economic interests absent an agreement, or that defendants possessed a strong common motive to conspire." *Id.* at 41a-42a. "[O]n a motion to dismiss[,] the Court may properly draw these background assumptions only from the facts pleaded in the complaint and the relevant statute, and may

rely only on such background facts about the market and its history that are appropriate for judicial notice." *Id.* at 46a.

Plaintiffs failed to satisfy the applicable standard. With regard to plaintiffs' allegation that defendant ILECs conspired to keep CLECs out of their individual markets, plaintiffs explicitly conceded that "it is in each ILEC's individual economic interest to attempt to keep CLECs out of its market." *Id.* at 48a. While each defendant might gain certain benefits from *other* incumbents' efforts to exclude CLECs, "[n]o agreement would be necessary for all ILECs to be relatively certain to reap the alleged added benefits to be gained from parallel action" and "the motives that plaintiffs have proffered do not provide any basis to infer" that defendants' conduct was the result of agreement. *Id.* at 50a.

With regard to plaintiffs' allegation that defendants agreed not to expand meaningfully into each others' territories, the court noted that "geographic segregation . . . might be enough . . . to support an inference of conspiracy, in most industries, where one could view the defendants as non-monopolistic competitors who had . . . apparently arranged [the market] into a pattern of territorial fiefdoms." *Id.* at 47a. In this case, however, the Bell companies were "given monopolies in their respective territories" and were "prevented from [competing prior to 1996] by the entry barriers protecting each" company's territory. *Id.*

The court carefully reviewed the history of regulation, the terms of the statute, and the allegations of the complaint – particularly those describing the difficulties faced by new local service entrants – and concluded that "[f]or an ILEC to compete as a CLEC in an adjoining ILEC's territory would not be simply to extend their existing business into a neighboring region, but rather would be to invest in undertaking an entirely different kind of business." *Id.* at 57a. "Given the obstacles to becoming a successful CLEC, . . . [i]t is no more surprising, and raises no more inference of concerted action, that the ILECs have not gone into business as

CLECs than that they have all collectively failed to enter some other line of business." *Id.* The court thus held that, "[i]n light of the structure of the market as evidenced by the allegations in the Amended Complaint and the provisions of the 1996 Act, . . . it is apparent that this conduct is also attributable to defendants' individual economic interests, and therefore does not raise an inference of conspiracy." *Id.* at 51a.

D. The Court of Appeals' Opinion

The Second Circuit reversed, concluding that "the district court applied an incorrect standard for evaluating the defendants' motion to dismiss." Pet. App. 10a-11a. The court of appeals held that allegations of parallel conduct coupled with a bald assertion that the defendants were participants in a "conspiracy" are sufficient to state a claim under Section 1. Accordingly, the court of appeals said that it did not even need to address the district court's conclusion that the facts alleged in the complaint failed to support any inference that the alleged parallel conduct was the result of a conspiracy rather than independent action in each defendant's economic self-interest. *See id.*

The court of appeals acknowledged that "a bare bones statement of conspiracy . . . without any supporting facts permits dismissal." *Id.* at 16a (internal quotation marks omitted). And the court stated that "[t]he factual predicate that is pleaded does need to include conspiracy among the realm of plausible possibilities." *Id.* at 19a (footnote omitted). But the court held that "a pleading of facts indicating parallel conduct by the defendants can suffice to state a plausible claim of conspiracy." *Id.* at 25a. "[T]o rule that allegations of parallel anticompetitive conduct fail to support a plausible conspiracy claim," the court stated, "a court would have to conclude that there is *no set of facts* that would permit a plaintiff to demonstrate that the particular parallelism asserted was the product of collusion rather than coincidence." *Id.* (emphasis added). *See id.* at 10a-11a.

Accordingly, the court of appeals held that "plaintiffs have satisfied their burden at the pleading stage." *Id.* at 30a. Devoting approximately three pages of the 43-page slip opinion to the issue, the court concluded that, "[w]hile the amended complaint does not identify specific instances of conspiratorial conduct or communications, it does set forth the temporal and geographic parameters of the alleged illegal activity and the identities of the alleged key participants," by which the court of appeals meant only that the conspiracy was alleged to have begun "around the time the Telecommunications Act became law," that it allegedly affected the entire contintental United States, and that the "alleged key participants" were the named corporate defendants. *Id.* at 31a.

The court of appeals said it was "mindful that a balance is being struck here, that on one side of that balance is the sometimes colossal expense of undergoing discovery, that such costs themselves likely lead defendants to pay plaintiffs to settle what would ultimately be shown to be meritless claims, that the success of such meritless claims encourages others to be brought, and that the overall result may well be a burden on the courts and a deleterious effect on the manner in which and efficiency with which business is conducted." *Id.* at 30a. But the court held that, "[i]f that balance is to be recalibrated, . . . it is Congress or the Supreme Court that must do so." *Id.*

The Second Circuit denied rehearing on January 3, 2006. *See id.* at 59a-60a. The Court granted certiorari on June 26, 2006.

SUMMARY OF ARGUMENT

Rule 8 requires pleading of facts – not mere conclusory assertions – "showing that the pleader is entitled to relief." Fed. R. Civ. P. 8(a). To state a claim for relief under Section 1 of the Sherman Act, a plaintiff must allege, first of all, that the defendants entered into a "contract, combination . . . or conspiracy" in restraint of trade. 15 U.S.C. § 1. Where, as here, a plaintiff alleges that the defendants have engaged in parallel conduct, and claims that the parallel conduct was the result of a conspiracy, a complaint is properly dismissed unless the facts alleged support, either directly or through a process of reasonable inference, the "conspiracy" conclusion.

I. A. The principles governing a district court's evaluation of a motion to dismiss for "failure to state a claim upon which relief can be granted," Fed. R. Civ. P. 12(b)(6), are settled and apply to this antitrust complaint. The court "must accept as true all the *factual* allegations in the complaint." *Leatherman v. Tarrant County Narcotics Intelligence & Coordination Unit*, 507 U.S. 163, 164 (1993) (emphasis added). By the same token, the court is "not bound to accept as true a legal conclusion couched as a factual allegation." *Papasan v. Allain*, 478 U.S. 265, 286 (1986).

Whether a complaint's factual allegations are sufficient to show that "the pleader is entitled to relief" must be judged in light of the substantive legal standards governing the claim. "[T]he appropriate level of generality for a pleading depends on the particular issue in question or the substantive context of the case before the court." 5 Charles A. Wright & Arthur R. Miller, *Federal Practice and Procedure* § 1218, at 273 (3d ed. 2004) ("Wright & Miller"). What constitutes adequate allegations of fact depends on what "plaintiffs[] need to *prove*" to state a claim for relief. *Dura Pharms., Inc. v. Broudo*, 544 U.S. 336, 346 (2005).

B. A complaint under Section 1 must include sufficient *factual* allegations to support the conclusion that the defendants conspired. A plaintiff may satisfy this requirement

either by making "direct allegations" sufficient to support a claim of conspiracy or by making "allegations from which an inference fairly may be drawn by the district court that evidence on these material points will be available and introduced at trial." 5 Wright & Miller § 1216, at 220-27. A bare assertion that defendants conspired, however, is not enough. *See DM Research, Inc. v. College of Am. Pathologists*, 170 F.3d 53, 55, 56 (1st Cir. 1999) (Boudin, J.); *see also Associated Gen. Contractors of California, Inc. v. California State Council of Carpenters*, 459 U.S. 519, 528 n.17 (1983) ("[A] district court must retain the power to insist upon some specificity in pleading before allowing a potentially massive factual controversy to proceed.").

C. Where a plaintiff alleges parallel conduct and asserts, without additional supporting factual allegations, that such conduct is the result of conspiracy, the district court must determine whether the inference is warranted, taking all factual allegations as true and drawing all inferences from those facts favorably to the plaintiff. In drawing such inferences, the district court must be mindful of underlying substantive antitrust standards, which recognize that, in most circumstances, parallel conduct does *not* support an inference of conspiracy. What is required are factual allegations "'that tend[] to exclude the possibility' that the alleged conspirators acted independently." *Matsushita Elec. Indus. Co. v. Zenith Radio Corp.*, 475 U.S. 574, 588 (1986) (quoting *Monsanto Co. v. Spray-Rite Serv. Corp.*, 465 U.S. 752, 764 (1984)).

D. The standard articulated by the Second Circuit for judging the sufficiency of allegations of parallel conduct is incorrect. That collusion is one "plausible possibilit[y]" underlying parallel conduct does not mean that independent action is not also plausible, or even *more* plausible. The Second Circuit's mere-plausibility standard does not comport with the standard for antitrust conspiracy because it does not require facts that "'tend[] to exclude'" the possibility that defendants acted independently. *Matsushita*, 475 U.S. at 588 (quoting *Monsanto*, 465 U.S. at 764). Moreover, the Second

Circuit's focus on facts that a plaintiff may yet uncover, rather than on facts actually alleged in the complaint, violates a basic principle governing motions to dismiss. "It is not . . . proper to assume that the [plaintiff] can prove facts that it has not alleged." *Associated Gen. Contractors*, 459 U.S. at 526 & n.11.

II. The district court correctly dismissed the complaint for failure to state a claim. The complaint contained no direct factual allegations to support a claim that defendants conspireed. Instead, the complaint relied solely on the inferences to be drawn from two categories of allegedly parallel conduct: (1) inadequate assistance to CLECs and (2) failure to compete "meaningfully" in other territories as CLECs. Neither of these general allegations supports an inference of collusion.

A. The allegation that defendants failed to comply fully with the network-sharing obligations of the 1996 Act, *see* JA 23-24 (Am. Compl. ¶ 47), does not support an inference of collusion because there is an obvious unilateral explanation for the conduct, which the complaint's allegations did not tend to exclude. There is nothing suspicious from the point of view of antitrust law about an incumbent's alleged reluctance to facilitate CLECs' efforts to take away the incumbent's customers. Indeed, as this Court has recognized, the dealing with rivals that the 1996 Act requires is not something that an incumbent would ever "voluntarily" undertake. *Trinko*, 540 U.S. at 409; *see id.* at 410.

B. The allegation that defendants failed to compete "meaningfully" in each others' traditional local-service territories is likewise insufficient to support an inference of conspiracy. There are numerous unilateral explanations for decisions *not* to enter, or not to enter "meaningfully." Accordingly, "parallel decisions by business firms not to enter new markets" have no tendency to exclude such unilateral explanations. Phillip E. Areeda & Herbert Hovenkamp, *Antitrust Law* ¶ 307d, at 155 (Supp. 2006) ("Areeda & Hovenkamp");

see also 6 Areeda & Hovenkamp ¶ 1410c, at 64 (2d ed. 2003) (mutual failure of rivals to enter each others' territories not indicative of agreement).

This is particularly clear in this case. The allegations in the amended complaint themselves recognized that "being a CLEC in another ILEC's territory is an entirely different business than being an ILEC." Pet. App. 51a. While the incumbent carrier "controls and maintains . . . telecommunications infrastructure," new entrants are "dependent on [their] relationship with the local ILEC." *Id.* at 51a-52a. The profitability of the new entrant would therefore "depend in substantial part on the terms that can be negotiated with the ILEC . . . and whether the ILEC fulfills its obligations" (*id.* at 52a), which – according to plaintiffs' central allegation – the ILEC would resist doing.

Beyond this, the courts repeatedly vacated the UNE-P regime until the FCC finally eliminated it. The lack of regulatory certainty provided an additional reason not to pursue a strategy based on the UNE-P regime. Those facts – from plaintiffs' own complaint – demonstrate that a decision not to devote scarce resources to the risky enterprise of becoming a CLEC is perfectly rational and explicable on its own terms for each defendant acting entirely out of independently determined self-interest.

ARGUMENT

I. TO STATE A CLAIM UNDER SECTION 1, A PLAINTIFF MUST ALLEGE FACTS SUFFICIENT TO SUPPORT THE CONCLUSION THAT DEFENDANTS CONSPIRED

This Court's decisions establish two fundamental pleading rules that bear decisively on this case. First, a complaint must allege facts, not merely conclusions, that show the plaintiff is entitled to relief under the governing substantive law. Second, it is the facts alleged, not unalleged facts that the plaintiff might later prove, that must support the claim to relief. *See Associated Gen. Contractors*, 459 U.S. at 526 ("It is not . . . proper to assume that the [plaintiff] can prove facts that it has not alleged."); *Wilson v. Schnettler*, 365 U.S. 381, 383 (1961).

As applied to a Section 1 complaint, those requirements demand more than allegations of parallel conduct (which is legal and commonplace in our economy) plus the conclusory label "conspiracy." They demand facts that themselves tend to exclude the likelihood that the conduct was unilateral. *See Matsushita*, 475 U.S. at 588; *Monsanto*, 465 U.S. at 764. The Second Circuit incorrectly abandoned the requirement of such allegations and instead allowed costly litigation to proceed based merely on the possibility that unalleged facts might yet support the claim for relief. That decision is wrong as a matter of pleading law and harmful as a matter of antitrust policy.

A. Rule 8 Requires Pleading of Facts, Not Mere Conclusory Assertions, To Support a Plaintiff's Claim

Rule 8 requires that each "pleading which sets forth a claim for relief" must contain "a short and plain statement of the claim showing that the pleader is entitled to relief." Fed. R. Civ. P. 8(a)(2). When a defendant files a motion pursuant to Rule 12(b)(6) to test the legal sufficiency of a pleading, courts distinguish between the *facts* alleged in the complaint – which must be accepted as true for purposes of evaluating

whether the complaint "state[s] a claim upon which relief can be granted," Fed. R. Civ. P. 12(b)(6); *see Leatherman*, 507 U.S. at 164 – and "allegations that are merely conclusory, unwarranted deductions of fact, or unreasonable inferences," *Manufactured Home Communities Inc. v. City of San Jose*, 420 F.3d 1022, 1035 (9th Cir. 2005) (internal quotation marks omitted) – which need not be accepted.[1]

This distinction between well-pleaded facts, on the one hand, and conclusory assertions and inferences, on the other, is indispensable to enforce the requirement that a complaint "provide the defendant with 'fair notice of what the plaintiff's claim is and the grounds upon which it rests.'" *Dura*, 544 U.S. at 346 (quoting *Conley v. Gibson*, 355 U.S. 41, 47 (1957)). As Judge Boudin explained in *DM Research*:

> [T]he price of entry, even to discovery, is for the plaintiff to allege a *factual* predicate concrete enough to warrant further proceedings, which may be costly and burdensome. Conclusory allegations in a complaint, if they stand alone, are a danger sign that the plaintiff is engaged in a fishing expedition.

170 F.3d at 55. As the Wright & Miller treatise explains, Rule 8's rejection of the detailed pleading of evidence required under the codes was not intended to eliminate the requirement that a complaint must contain factual allegations on "every material point necessary to sustain a recovery." 5 Wright & Miller § 1216, at 220-27. *See also* Brief of Mastercard International Inc. and Visa U.S.A. Inc. as *Amici Curiae* in Support of Petitioners at 4-9 (filed Aug. 25, 2006).

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[1] *See also, e.g., Papasan*, 478 U.S. at 286; *Stachowski v. Town of Cicero*, 425 F.3d 1075, 1078 (7th Cir. 2005); *Veney v. Wyche*, 293 F.3d 726, 730 (4th Cir. 2002) (court not required "to accept as true allegations that are merely conclusory, unwarranted deductions of fact, or unreasonable inferences" or "allegations that contradict matters properly subject to judicial notice") (internal quotation marks omitted); *Dry v. United States*, 235 F.3d 1249, 1255 (10th Cir. 2000); *Doug Grant, Inc. v. Greate Bay Casino Corp.*, 232 F.3d 173, 184 (3d Cir. 2000); *In re Sofamor Danek Group, Inc.*, 123 F.3d 394, 400 (6th Cir. 1997).

Whether a complaint's allegations are sufficient under this standard must be judged in light of the substantive law governing the plaintiff's claim. "[T]he appropriate level of generality for a pleading depends on the particular issue in question or the substantive context of the case before the court." 5 Wright & Miller § 1218, at 273. This Court's decisions illustrate the application of this principle.

For example, the allegation that a defendant's conduct had an effect on interstate commerce sufficient to implicate the Sherman Act should rarely be controversial, because that requirement is not demanding. *See Summit Health, Ltd. v. Pinhas*, 500 U.S. 322, 331 (1991); *United States v. Employing Plasterers Ass'n of Chicago*, 347 U.S. 186, 189 (1954). By contrast, in a case where a plaintiff claims a violation of a constitutional right, this Court has required – under ordinary Rule 8 standards – factual allegations that are not merely conclusory. Thus, in *Papasan*, the plaintiffs alleged that they had been denied a "minimally adequate education," but the Court held that it was "not bound to credit and may disregard the allegation." 478 U.S. at 286. The Court noted:

> The petitioners do not allege that schoolchildren in the Chickasaw Counties are not taught to read or write; they do not allege that they receive no instruction on even the educational basics; they allege no actual facts in support of their assertion that they have been deprived of a minimally adequate education.

Id. Because such facts were critical to the resolution of the question whether the plaintiffs had a claim upon which relief could be granted, the Court would not assume their existence in the absence of a proper allegation.

Other recent cases illustrate the principle in a variety of contexts. For example, in *Anza v. Ideal Steel Supply Corp.*, 126 S. Ct. 1991 (2006), the plaintiff alleged that the defendants' predicate acts were "directed at" and "directly injure[d]" the plaintiff. Joint Appendix at 16 (Compl. ¶ 49), *Anza v. Ideal Steel Supply Corp.*, No. 04-443 (U.S. filed Jan.

12, 2006); *see also, e.g.*, *id.* at 5 (Compl. ¶ 1) (plaintiff's lost business "direct effect" of challenged conduct); *id.* at 7 (Compl. ¶ 6) (scheme "directly injures" plaintiff). The Court disregarded these assertions in holding, on a motion to dismiss, that the complaint's allegations were insufficient to meet the direct-injury requirement for a claim under the RICO statute. Notwithstanding the plaintiff's conclusory assertion, the Court concluded that the factual allegations indicated that "[t]he *direct* victim of this conduct was the State of New York, not Ideal." *Anza*, 126 S. Ct. at 1997 (emphasis added). That conclusion was "confirmed by considering the directness requirement's underlying premises" – that is, "the difficulty that can arise when a court attempts to ascertain the damages caused by some remote action." *Id.*

In *Dura*, a unanimous Court similarly held insufficient, on a motion to dismiss, the plaintiffs' assertion that, as a result of the defendants' misrepresentations, the plaintiffs had "paid artificially inflated purchase prices" and were thereby "damage[d]." 544 U.S. at 347; *see also* Joint Appendix at 55a (Compl. ¶ 37), *Dura Pharms., Inc. v. Broudo*, No. 03-932 (U.S. filed Sept. 13, 2004) (alleging that "[p]ublic investors, who purchased Dura stock at prices inflated by the false representations . . . , have suffered millions in damages"). Applying Rule 8 standards, the Court held that the complaint's assertion failed in light of the requirement that a plaintiff seeking to recover for securities fraud must prove economic loss and proximate cause to recover. *See* 544 U.S. at 346 ("Our holding about plaintiffs' need to *prove* proximate causation and economic loss leads us also to conclude that the plaintiffs' complaint here failed adequately to *allege* these requirements."). The Court reasoned:

> [I]t should not prove burdensome for a plaintiff who has suffered an economic loss to provide a defendant with some indication of the loss and the causal connection that the plaintiff has in mind. At the same time, allowing a plaintiff to forgo giving any indication of the economic loss and proximate cause that the

> plaintiff has in mind would bring about harm of the very sort the statutes seek to avoid

– that is, litigation of groundless claims. *Id.* at 347; *see also* Areeda & Hovenkamp ¶ 307, at 156 n.17 ("*Dura* itself . . . was applying ordinary, not heightened, pleading rules.").

And, in *Trinko*, likewise decided on a motion to dismiss, the Court similarly held the required exclusionary-conduct allegation to be legally insufficient, notwithstanding the plaintiff's assertion that the defendant's failure to provide adequate access to network facilities had "no valid business reason" and constituted "exclusionary and anticompetitive behavior." Joint Appendix at 46, 47 (Am. Compl. ¶¶ 52, 57), *Verizon Communications Inc. v. Law Offices of Curtis V. Trinko, LLP*, No. 02-682 (U.S. filed May 23, 2003) ("*Trinko* JA"). Instead, the Court looked to the complaint's *factual* allegations and took judicial notice of certain obvious facts, including that "unbundled elements . . . exist only deep within the bowels of Verizon; [and that] they are brought out on compulsion of the 1996 Act and offered not to consumers but to rivals, and at considerable expense and effort." *Trinko*, 540 U.S. at 410. It then concluded that an alleged refusal to deal in these circumstances did not state a claim under Section 2 of the Sherman Act.

B. A Conclusory Allegation of "Conspiracy" Is Insufficient To State a Claim Under Section 1

1. In this case, the governing antitrust law required that plaintiffs allege facts sufficient to support the conclusion that the conduct alleged was the result of a conspiracy. *Trinko* establishes that a unilateral failure to share network elements, as required by the 1996 Act, does not violate the antitrust laws. Nor, of course, would a unilateral decision not to enter a particular market. The existence of a conspiracy – the element of agreement – is a critical element in distinguishing between lawful and potentially unlawful conduct.

In this legal context, the lower courts have rightly insisted that plaintiffs do more than make "bare bones" averments of conspiracy. *Heart Disease Research Found. v. General Motors Corp.*, 463 F.2d 98, 100 (2d Cir. 1972); *see also Tal v. Hogan*, 453 F.3d 1244, 1261 (10th Cir. 2006); *DM Research*, 170 F.3d at 55-56; *Estate Constr. Co. v. Miller & Smith Holding Co.*, 14 F.3d 213, 221 (4th Cir. 1994); *Lombard's, Inc. v. Prince Mfg., Inc.*, 753 F.2d 974, 975 (11th Cir. 1985). *See generally* Christopher M. Fairman, *The Myth of Notice Pleading*, 45 Ariz. L. Rev. 987, 1036 (2003) (noting a judicial "consensus" under which "[c]onclusory allegations [of conspiracy] are consistently rejected").

A pleading of conspiracy requires factual allegations that directly support the existence of an agreement or, failing that, facts that support an inference that defendants conspired. *See* 5 Wright & Miller § 1216, at 220-27. As the First Circuit held in affirming dismissal of a Section 1 claim:

> [T]erms like "conspiracy," or even "agreement," are border-line: they might well be sufficient in conjunction with a more specific allegation – for example, identifying a written agreement or even a basis for inferring a tacit agreement – but a court is not required to accept such terms as a sufficient basis for a complaint.

DM Research, 170 F.3d at 56 (citation omitted).

Drawing the line between a conclusory allegation and a factual allegation requires exercise of sound judicial judgment. As this Court has held, Rule 8 and Rule 12 preserve courts' power "to insist upon some specificity in pleading." *Associated Gen. Contractors*, 459 U.S. at 528 n.17; *see also Dura*, 544 U.S. at 347 (failing to require adequate factual allegations "would permit a plaintiff 'with a largely groundless claim to simply take up the time of a number of other people, with the right to do so representing an *in terrorem* increment of the settlement value, rather than a reasonably founded hope that the [discovery] process will reveal relevant evi-

dence'") (quoting *Blue Chip Stamps v. Manor Drug Stores*, 421 U.S. 723, 741 (1975)) (alteration added by *Dura* Court); *Reiter v. Sonotone Corp.*, 442 U.S. 330, 345 (1979) (encouraging district courts to "use the tools available" to avoid "administrative chaos, class-action harassment, or 'windfall' settlements"); *Davis v. Passman*, 442 U.S. 228, 238 n.15 (1979) ("It is not enough to indicate merely that the plaintiff has a grievance but sufficient detail must be given so that the defendant, and the court, can obtain a fair idea of what the plaintiff is complaining, and can see that there is some legal basis for recovery") (internal quotation marks omitted).

2. The Court's decision in *Swierkiewicz v. Sorema N.A.*, 534 U.S. 506 (2002), does not require a district court to accept a conclusory allegation of antitrust conspiracy without supporting facts. The Court there reversed dismissal of the plaintiff's claim of employment discrimination, noting that the complaint "detailed the events leading to his termination, provided relevant dates, and included the ages and nationalities of at least some of the relevant persons involved." *Id.* at 514. The contested issue was not whether the plaintiff had sufficiently pleaded the required conduct; rather, the Court held that the lower courts erred by requiring that the plaintiff go beyond his plain allegation that he was fired "on account of" his age and national origin ("motivating factors"), Joint Appendix at 25a, 27a (Am. Compl. ¶¶ 20, 37), *Swierkiewicz v. Sorema N.A.*, No. 00-1853 (U.S. filed Nov. 16, 2001), and present facts to make out a *prima facie* case of discrimination under the optional framework for presenting and evaluating evidence laid out in *McDonnell Douglas Corp. v. Green*, 411 U.S. 792 (1973). This Court rejected the requirement, noting that "the *McDonnell Douglas* framework does not apply in every employment discrimination case," and that the plaintiff might be able to provide "direct evidence of discrimination." *Swierkiewicz*, 534 U.S. at 511.

The allegation of "conspiracy," without any facts suggestive of it, presents a critically different problem from the allegation of discriminatory motive in the context of the

specific facts alleged in *Swierkiewicz*. Indeed, plaintiffs themselves, like the Second Circuit (Pet. App. 16a), admitted that a naked "conspiracy" allegation would *not* suffice. *See* JA 94-95 (Dist. Ct. 8/1/03 Tr. 21). Unlike the charge of discriminatory motive in *Swierkiewicz* (about a specific firing of a specific employee), the "conspiracy" label here adds nothing to the underlying factual allegations about parallel conduct. The problem is not failure to reveal the evidentiary basis for a legally sufficient factual allegation. It is that, without flesh on the bare bones, an assertion of conspiracy fails to reveal a factual predicate sufficient to satisfy Rule 8 standards.

This inquiry into the adequacy of a complaint's allegations of antitrust conspiracy cannot be side-stepped by positing that a plaintiff might (despite the absence of direct or inferential factual allegations) be able to prove conspiracy after discovery. *Cf.* Pet. App. 26a; *see also infra* pp. 28-29. That is simply to argue that, despite the failure to "show that the 'pleader is entitled to relief'" – the standard under Rule 8 – a complaint should be permitted to proceed so long as a plaintiff claims that "there is 'reason to believe that, upon evidence which may be disclosed by discovery, the pleader may be entitled to relief.'" Fleming James, Jr., *et al.*, *Civil Procedure* § 3.6, at 189 (5th ed. 2001). Rule 8 forecloses that argument.

C. When a Complaint Alleges Conspiracy Based on Parallel Conduct, the Factual Allegations Must Support an Inference that the Defendants Conspired

1. Substantive antitrust law draws a sharp distinction between concerted action prohibited by Section 1 and parallel but unilateral conduct, which Section 1 does not address. "[T]his Court has never held that proof of parallel business behavior conclusively establishes agreement or, phrased differently, that such behavior itself constitutes a Sherman Act offense." *Theatre Enters., Inc. v. Paramount Film Distrib.*

Corp., 346 U.S. 537, 541 (1954). *See also Brooke Group Ltd. v. Brown & Williamson Tobacco Corp.*, 509 U.S. 209, 227 (1993)

Accordingly, allegations of parallel conduct cannot by themselves satisfy the agreement element of Section 1. Parallel conduct is to be expected when similarly situated competitors react to comparable market conditions. Accordingly, to state a claim for relief, it is not enough for a plaintiff to allege that defendants engaged in parallel conduct; there must be sufficient *factual* allegations to support the conclusion that defendants conspired. As the district court correctly held, the pleaded facts must allow the court to "distinguish between conduct that represents the natural convergence of competitors' market behavior, and conduct that appears to have been taken pursuant to an agreement." Pet. App. 41a.

In drawing that distinction, the district court properly relied on the basic principle articulated in *Matsushita* and *Monsanto* that "a plaintiff seeking damages for a violation of § 1 must present evidence 'that tends to exclude the possibility' that the alleged conspirators acted independently." *Matsushita*, 475 U.S. at 588 (quoting *Monsanto*, 465 U.S. at 764). As the courts of appeals have uniformly held in evaluating claims of horizontal conspiracy, such allegations must tend to show "that the defendants' behavior would not be reasonable or explicable (i.e., not in their legitimate economic self-interest) if they were not conspiring to fix prices or otherwise restrain trade." *Williamson Oil Co. v. Philip Morris USA*, 346 F.3d 1287, 1301 (11th Cir. 2003) (internal quotation marks omitted); *see, e.g., In re Flat Glass Antitrust Litig.*, 385 F.3d 350, 360-61 (3d Cir. 2004), *cert. denied*, 544 U.S. 948 (2005); *Viazis v. American Ass'n of Orthodontists*, 314 F.3d 758, 762, 764 (5th Cir. 2002); *Blomkest Fertilizer, Inc. v. Potash Corp. of Saskatchewan*, 203 F.3d 1028, 1033 (8th Cir. 2000) (en banc); *In re Citric Acid Litig.*, 191 F.3d 1090, 1100 (9th Cir. 1999); *In re Brand Name Prescription Drugs Antitrust Litig.*, 186 F.3d 781, 787-88 (7th Cir. 1999) (Posner, J.); *see also Toys "R" Us, Inc. v. FTC*, 221 F.3d 928, 936 (7th Cir.

2000). A complaint that seeks to state a claim under Section 1 where the only facts alleged describe parallel conduct and attendant market circumstances must – taking the alleged facts as true and drawing all inferences favorable to the plaintiff – meet this "tends-to-exclude" standard. *See, e.g., Cayman Exploration Corp. v. United Gas Pipe Line Co.*, 873 F.2d 1357, 1361 (10th Cir. 1989). This is the standard that the district court applied. *See* Pet. App. 46a.

Requiring allegations that support an inference that defendants acted against their self-interest, but for the existence of an agreement, reflects both basic antitrust logic and important policy concerns. If defendants acted in their individual self-interest, then there is no reason, based simply on parallel conduct, to infer the existence of such an agreement. *See First Nat'l Bank v. Cities Serv. Co.*, 391 U.S. 253, 279-80 (1968); *Matsushita*, 475 U.S. at 587 (where defendant's "refusal to deal was consistent with the defendant's independent interest, the refusal to deal could not by itself support a finding of antitrust liability").

Furthermore, to allow a plaintiff to plead a claim under Section 1 based on parallel conduct – without supporting facts tending to exclude the possibility of independent action – would be to subject a defendant to litigation for alleged conduct that is consistent with legitimate business judgment, placing a heavy tax on ordinary business activity. *See* Brief of *Amici Curiae* Economists in Support of Petitioners at 16-18 (filed Aug. 25, 2006). To allow too-easy inference of conspiracy based on parallel conduct would "deter or penalize perfectly legitimate conduct" and hence "both inhibit management's exercise of independent business judgment and emasculate the terms of the statute." *Monsanto*, 465 U.S. at 763-64 (internal quotation marks omitted).

2. While *Matsushita* was decided on summary judgment, the standard that Judge Lynch applied comports with the proper function of a motion to dismiss.

The critical difference is the most obvious one: on a motion to dismiss, a complaint's factual allegations are accepted as true and defendants may introduce only judicially noticeable facts in their defense. *See Leatherman*, 507 U.S. at 164. By contrast, on summary judgment, the plaintiff must point to "sufficient *evidence* supporting the claimed factual dispute . . . to require a jury or judge to resolve the parties' differing versions of the truth at trial." *Anderson v. Liberty Lobby, Inc.*, 477 U.S. 242, 249 (1986) (emphasis added; internal quotation marks omitted). The purpose of a motion for summary judgment is thus to test the sufficiency of the plaintiff's evidence. The purpose of the motion to dismiss, by contrast, is to determine whether – accepting the allegations of the complaint as true – the plaintiff has a legally cognizable claim that justifies starting the expensive machinery of litigation.

Courts have rightly insisted upon the importance of summary judgment as a mechanism to promote judicial efficiency. But the observation applies with even greater force where a complaint fails to establish a legally cognizable basis for a claim, even taking its factual allegations as true. The court of appeals acknowledged the "well-founded concern" about "condemn[ing] defendants to potentially limitless 'fishing expeditions' – discovery pursued just 'in case anything turn[s] up' – in hopes, perhaps, of a favorable settlement in any event." Pet. App. 27a (footnotes omitted; second alteration in original); *see also* 6 James Wm. Moore, *et al.*, *Moore's Federal Practice* ¶ 26.46[1], at 26-146.24 (3d ed. 2003) ("antitrust cases have become known as 'serpentine labyrinths' in which discovery is a 'bottomless pit' "). There is no justification for allowing such litigation to proceed where a complaint has failed to provide a factual basis for any claim for relief. *See also* Brief of the Chamber of Commerce of the United States of America, *et al.*, as *Amici Curiae* in Support of Petitioners at 18-26 (filed Aug. 25, 2006).

The Federal Rules "shall be construed and administered to secure the just, speedy, and inexpensive determination of every action." Fed. R. Civ. P. 1. Proper application of substantive antitrust standards and the requirement that plaintiffs plead facts sufficient to make out a legally cognizable claim serve this overriding goal.

D. The Second Circuit's Standard, Which Assumes the Existence of Facts Not Alleged, Is Inconsistent with Rule 8 and Substantive Antitrust Standards

The Second Circuit's standard for judging the sufficiency of a complaint conflicts with the Rule 8 principles and substantive antitrust law requirements set forth above.

The court began by holding that, at the pleading stage, a plaintiff "must allege only the existence of a conspiracy and a sufficient supporting factual predicate on which that allegation is based." Pet. App. 25a. But, in giving content to the latter requirement, the court held that such a factual predicate would merely need to "include conspiracy among the realm of 'plausible' possibilities." *Id.* And, in the specific context of parallel-conduct allegations, the court held that such allegations are insufficient only when "there is *no set of facts* that would permit a plaintiff to demonstrate that the particular parallelism asserted was the product of collusion rather than coincidence." *Id.* (emphasis added).

The court's holding is erroneous in two basic respects. First, it is inconsistent with the basic antitrust principle that parallel conduct provides no basis for inferring a conspiracy unless it tends to exclude the possibility of independent action. As the court itself recognized, a bare allegation of conspiracy, without supporting facts, is insufficient. Adding allegations of parallel conduct does not show that the plaintiff is entitled to relief, because parallel conduct is not unlawful or generally even suggestive of agreement. Instead, the allegations must support an inference of conspiracy under the applicable legal standard, which requires that the facts tend to exclude independent action as an equally likely (or even

more likely) explanation. The Second Circuit's standard, by contrast, would almost never permit dismissal of allegations of parallel conduct. It is almost never true that there is "no set of facts that would permit a plaintiff to demonstrate that the particular parallelism asserted was the product of collusion," because it is almost always possible that parties agreed, no matter how improbable such an agreement might be. *See DM Research*, 170 F.3d at 57.

Second, the court's standard is inconsistent with the principle of pleading law that "[i]t is not . . . proper to assume that the [plaintiff] can prove *facts that it has not alleged*." *Associated Gen. Contractors*, 459 U.S. at 526 & n.11 (emphasis added). It is true, as the Second Circuit suggested, that a plaintiff might nevertheless prove the existence of an improbable conspiracy through "direct[]" proof. Pet. App. 26a. But that suggestion, relying entirely on what *might* ultimately be "prove[d]," effectively wipes away any requirement that the complaint actually *allege* sufficient facts to state a claim. The Second Circuit has thus done precisely what this Court held is improper: it has allowed the complaint to proceed because collusion is a "'plausible' possibilit[y]" based on a "set of facts" *not* alleged. *Id.* at 25a.

Nor is the Second Circuit's decision consistent with *Conley*, despite the court's borrowing of the "no set of facts" language from that opinion. The Court's statement in *Conley* that a complaint should not be dismissed unless there is "no set of facts" that a plaintiff could prove in support of his claim does not mean that a court must hypothesize unalleged facts. *See, e.g.*, *Wilson*, 365 U.S. at 383 ("[i]n the absence of . . . an allegation [that the arrest was made without probable cause] the courts below could not, nor can we, assume that respondents arrested petitioner without probable cause"). That language means, instead, that, if a complaint's allegations make out a violation of a legal duty, neither the failure to identify the duty with particularity nor the possibility of defenses will defeat a claim. *See Conley*, 355 U.S. at 46-47. The Court *later* addressed the question whether the complaint

set forth sufficiently "*specific* facts" in support of its "general allegations of discrimination." *Id.* at 47 (emphasis added). And it held – much as the Court did in *Swierkiewicz* – that an allegation that the union had failed to represent the plaintiffs because of their race under specifically alleged circumstances was sufficient to place the defendants on notice of both the claim and its factual basis. *See id.* The allegations here do not meet that standard.

II. THE COMPLAINT'S ALLEGATIONS FAIL TO SUPPORT AN INFERENCE OF CONSPIRACY UNDER THE PROPER LEGAL STANDARD

Plaintiffs sought to allege an agreement in restraint of trade not directly – by identifying collusive communications (in-person, written, electronic, or otherwise) or actions – but instead by specifying parallel marketplace conduct from which they seek an inference of agreement. The complaint is devoid of specifics regarding the participants, the time period, the terms of the agreement, the mechanism of enforcement, or any other facts that would permit defendants to investigate and defend against the charge. Instead, the allegation of conspiracy rests on "the absence of any meaningful competition between the [defendants] in one another's markets" and "the parallel course of conduct that each engaged in to prevent competition." JA 27 (Am. Compl. ¶ 51). Indeed, plaintiffs below implicitly disclaimed having made any "direct" allegations of conspiracy. Reply Brief for Plaintiffs-Appellants at 6 (2d Cir. filed May 26, 2004) ("2d Cir. Reply Br."). *See also* Pet. App. 31a ("the amended complaint does not identify specific instances of conspiratorial conduct or communications"). Plaintiffs instead relied solely on inferential or "circumstantial" allegations. 2d Cir. Reply Br. at 6. As a matter of basic pleading law, however, the district court was not required to accept such inferences.

The "presumption of antitrust conspiracy law" is "that the inference of a conspiracy is always unreasonable when it is based solely on parallel behavior that can be explained as the

result of the independent business judgment of the defendants." *Southway Theatres, Inc. v. Georgia Theatre Co.*, 672 F.2d 485, 494 (5th Cir. 1982). It makes perfect sense for an ILEC not to cooperate with CLECs seeking to take away its customers (as alleged), quite apart from whether other ILECs follow suit. Nor is there anything suspicious about an ILEC's failure to enter new markets as a CLEC in its own right (as alleged), where it would be dependent upon a vanishing scheme of regulatory subsidies. When there is an evident, common-sense unilateral explanation for the conduct as fully described in the complaint, and no allegations of furtive meetings, suspicious communications, or the like, the complaint does not state a claim of conspiracy.

A. The Claim that ILECs Resisted Costly and Burdensome Network-Sharing Duties Does Not Support an Inference of Conspiracy

The complaint's allegation that each defendant resisted CLEC efforts to take away customers using the ILEC's own facilities is perfectly consistent with the unilateral business interest of each defendant. Indeed, plaintiffs expressly conceded before the district court "that it is in each ILEC's individual economic interest to attempt to keep CLECs out of its market." Pet. App. 48a (citing Dist. Ct. 8/1/03 Tr. 29 (JA 98)). Moreover, the only parallel conduct alleged – "fail[ure] to provide the same quality of service to competitors that Defendants provide to their own retail customers"; "fail[ure] to provide access to operational support systems . . . on a nondiscriminatory basis"; "undue delays in the provisioning of unbundled elements"; and so on, JA 23-24 (Am. Compl. ¶ 47) – is the exact same conduct that provided the basis for plaintiff Twombly's earlier claim that one of the defendants had violated *Section 2*. In that case, the allegation was that such behavior enabled the ILEC to maintain a profitable monopoly. Plaintiffs (and counsel) thus effectively conceded there, too, that the alleged conduct serves the independent business interest of each defendant.

The basis for this unilateral interest is simple, and confirmed by plaintiffs' complaint and this Court's decisions. Plaintiffs expressly alleged that, had any ILEC cooperated with CLECs, entry would have been rapid and customers would have been lost to CLEC rivals. *See* JA 26-27 (Am. Compl. ¶ 50). The very purpose of the sharing obligations imposed by the 1996 Act was to "eliminate the monopolies enjoyed by the inheritors of AT&T's local franchises" by providing competitors access to the incumbent's network at cut-rate prices. *Verizon Communications Inc. v. FCC*, 535 U.S. 467, 476 (2002). As this Court recognized in *Trinko*, any rational competitor – all other things being equal – would prefer to sell directly to end customers at full retail prices, *see* 540 U.S. at 409; and, even if no customers were lost, it would prefer to reduce the substantial expenditures that the 1996 Act imposed, *see id.* at 410. There is, in short, a unilateral explanation for the conduct alleged that is obvious on the face of the complaint.

The complaint does nothing to exclude that explanation when it postulates that defendants had "compelling common motivations to . . . agree[]" not to cooperate with CLECs because "greater competitive inroads" into one defendant's territory would have "enhanced the likelihood that such a CLEC might present a competitive threat in other Defendants' territories as well" and "would have revealed the degree to which competitive entry by CLECs would have been successful." JA 26-27 (Am. Compl. ¶ 50). There are two decisive problems with reliance on this allegation as tending to exclude the possibility of unilateral conduct.

First, this allegation at most hypothesizes a possible advantage from agreement (while wholly ignoring the countervailing legal risks).[2] The possibility of benefits from agreement

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[2] One could always hypothesize *some* reason that agreement with competitors would bring some incremental advantage (reducing uncertainty concerning rivals' actions can always reduce downside risks), but that does not undermine the conclusion that the conduct is in the defendants'

does not logically – and thus cannot legally – tend to exclude a unilateral explanation evident from the complaint itself. Here, in particular, the hypothesized advantages from agreement are not only speculative and indirect, but actually depend upon the premise that each ILEC has a strong, independent reason to block in-region entry in its own territory. As the district court correctly observed, "[t]he asserted motivations to make an agreement . . . are not considerations that would affect [an ILEC's] initial decision as to whether or not to fight the CLECs in its own market." Pet. App. 49a. That alleged decision remains fully explained in unilateral terms.[3]

Second, and in any event, the asserted motivation to conspire is itself undercut by the evident lack of *need* to have any agreement to achieve the postulated benefit. As the district court explained, each defendant "could rationally expect that each of [the others] will reach the same conclusion . . . . No agreement would be necessary for all ILECs to be relatively certain to reap the alleged added benefits to be gained" from other defendants' comparable course of conduct. *Id.* at 49a-50a. The complaint, in short, does nothing to tend to exclude the unilateral explanation for the alleged anti-CLEC conduct – or, therefore, to support an inference of conspiracy.

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individual interest *absent* agreement. *See, e.g., Serfecz v. Jewel Food Stores*, 67 F.3d 591, 600-01 (7th Cir. 1995) ("The mere existence of mutual economic advantage, by itself, does not tend to exclude the possibility of independent, legitimate action and supplies no basis for inferring a conspiracy.").

[3] The complaint did not even allege that defendants followed *the same* non-compliance strategies; rather, the complaint very generally alleged that each of the defendants engaged in "one or more" of 12 categories of conduct, each described in vague terms. Thus, for all that appears in the complaint, each defendant was engaged in *different* (not parallel) conduct in its allegedly inadequate cooperation with CLECs.

B. The Claim that ILECs Did Not Meaningfully Enter Each Others' Traditional Service Territories Does Not Support an Inference of Conspiracy

The facts alleged in the complaint likewise fail to raise an inference, or suspicion, that an ILEC's alleged failure to compete "meaningfully" in the territory of another ILEC is attributable to anything but unilateral business judgment. Indeed, the facts alleged positively undermine any such inference.

Firms have multiple demands on scarce capital, new entry is always risky, and a firm can exploit only a small fraction of available opportunities. Where, as a result of historical accident or deliberate design, two firms operate in adjacent territories, the failure of one to compete in the other's region does not support an inference of agreement. As stated in the leading antitrust treatise, that would be true, even if each firm's decision depends in part on the possibility of retaliatory entry. *See* 6 Areeda & Hovenkamp ¶ 1410c, at 64 (failure of rivals to "sell in the other's area although each is capable of doing so" does not support inference of agreement).[4]

The inherent uncertainty of new entry is reflected in the rule of antitrust law that a plaintiff that claims to be a potential entrant is denied antitrust standing to challenge exclusionary conduct *unless* the plaintiff has taken "actual and

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[4] As this Court noted in *Brooke Group Ltd. v. Brown & Williamson Tobacco Corp.*, 509 U.S. 209 (1993), even where firms consciously act in parallel ways "by recognizing their shared economic interests," that process is "not in itself unlawful." *Id.* at 227; *see also Theatre Enters.*, 346 U.S. at 541; 6 Areeda & Hovenkamp ¶ 1433a, at 236 ("The courts are nearly unanimous in saying that mere interdependent parallelism does not establish the contract, combination, or conspiracy required by Sherman Act § 1."). Thus, even if each ILEC consciously decided not to invade its neighbor's territory, in order not to provoke retaliatory entry, there would be no reason to infer an unlawful agreement. That is particularly true here, where, as discussed below, the complaint itself acknowledged ample independent reasons for each ILEC to forgo such entry.

substantial affirmative steps toward entry, such as the consummation of relevant contracts and procurement of necessary facilities and equipment." *Andrx Pharms., Inc. v. Biovail Corp.*, 256 F.3d 799, 807 (D.C. Cir. 2001) (internal quotation marks omitted); *see also, e.g., In re Dual-Deck Video Cassette Recorder Antitrust Litig.*, 11 F.3d 1460, 1465 (9th Cir. 1993); *Out Front Productions, Inc. v. Magid*, 748 F.2d 166, 170 (3d Cir. 1984). That venerable limitation on standing makes sense precisely because it is so well understood that a variety of factors – not least the availability of more attractive opportunities elsewhere – may lead a firm to pass up what may appear to others to be a potentially profitable new venture. And that limitation underscores the inappropriateness of inferring agreement from the type of parallel *in*action alleged here.

Such an inference is particularly unwarranted in light of the facts that plaintiffs *did* allege – allegations that the district court properly took into account in determining whether the complaint stated a claim. *See, e.g., Sutton v. United Air Lines, Inc.*, 527 U.S. 471, 481 (1999); *Cleveland Bd. of Educ. v. Loudermill*, 470 U.S. 532, 547 (1985). As alleged in the complaint, there are fundamental differences between providing telephone service over a company's own network – as ILECs do – and reselling the communications infrastructure of another company – as CLECs are alleged to do. *See* JA 26 (Am. Compl. ¶ 47(*l*)). This makes the decision to enter new territory as a CLEC akin to a decision to undertake a new (if related) business activity, not merely to expand existing activities. *See* Pet. App. 51a, 54a. The alleged fact of dependence on the ILEC – and the knowledge that the ILEC has the means to limit entry – provides a fully adequate explanation of defendants' alleged refusal to embrace the CLEC opportunity.

Furthermore, the complaint itself admits that the UNE-P regime – upon which defendants allegedly had an incentive to rely – was subject to judicial review throughout the period. *See* JA 19 (Am. Compl. ¶ 35). The courts made it clear that

the UNE-P was on a shaky foundation from the start, and it was kept in place only temporarily between judicial vacaturs. It is hardly surprising that an individual defendant would make an independent business and legal judgment not to rely on an unstable regulatory regime, particularly a regime that it was itself challenging in the courts as unlawful.

The allegation that ILEC-as-CLEC entry was "an especially attractive business opportunity" in areas where one ILEC serves territories that border (or surround) the territory of another (JA 21 (Am. Compl. ¶ 40)) does not support the required inference of conspiracy. That allegation is by its terms deficient: it does *not* say that the nearby-entry opportunity is *more attractive than other business opportunities*. The allegation thus does not make the minimally necessary claim, namely, that defendants were acting against independent self-interest. The distinction between what plaintiffs alleged and what would be minimally necessary is critical. "Firms do not expand without limit and none of them enters every market that an outside observer might regard as profitable, or even a small portion of such markets." Areeda & Hovenkamp ¶ 307, at 155 (criticizing Second Circuit decision at issue here). Unless an ILEC judged the UNE-P opportunity to be the *best* use of scarce capital in the long-run – which the complaint did *not* allege – failure to pursue the opportunity entails no sacrifice and hence is not suggestive of anything but unilateral decisionmaking. *See* 6 Areeda & Hovenkamp ¶ 1415e, at 99-100 ("One must not characterize a firm's sacrifice of short-run interest in favor of long-run interest as contrary to its self-interest.").

In any event, the assertion that the ILEC-as-CLEC opportunity was "especially attractive" is merely an inference or characterization – and one that is contradicted by the complaint's factual allegations. *See Trinko*, 540 U.S. at 410 (refusing to accept plaintiff's assertion that failure to provide access to network facilities had "no valid business reason," *Trinko* JA at 47 (Am. Compl. ¶ 57)). The complaint here admitted that ILECs, as new entrants, would face substantial

obstacles, because each ILEC "possess[es] the *exclusive and sole source of entry into its own local telephone . . . market.*" JA 26 (Am. Compl. ¶ 47(*l*)) (emphasis added). Moreover, "being a CLEC is an extraordinarily difficult enterprise" because "ILECs have been obstructionist i[n] providing CLECs with the tools necessary to engage in business." Pet. App. 54a. As alleged in the complaint, "the ILEC-as-CLEC is no different from any other CLEC" with regard to these factors. *Id.*

Plaintiffs cite the statement of Qwest CEO Richard Notebaert – who said that competing as a CLEC "'might be a good way to turn a quick dollar but that doesn't make it right,'" JA 22 (Am. Compl. ¶ 42) – as support for the claim that competition as a CLEC presented an attractive business opportunity. As the district court rightly observed, Mr. Notebaert's statements "suggest only that he did not consider becoming a CLEC to be a sound long-term business plan" because "the legal landscape in which CLECs operate could have changed at any time." Pet. App. 56a.[5] In fact, that prediction was borne out: the UNE-P regime is long gone, and those CLECs that invested in UNE-P competition have seen that business model go into steep decline. *See supra* pp. 4-5.

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[5] Later in the same article quoted by plaintiffs, Mr. Notebaert, while discussing the regulatory regime that requires incumbent firms to sell network elements to rivals at wholesale prices, is quoted as saying: "'I don't think it's a sustainable economic model.' . . . 'It's just a nuts pricing model.'" Jon Van, *Ameritech Customers Off Limits: Notabaert*, Chi. Trib., Oct. 31, 2002, at Business p.1 (JA 42). Moreover, another article cited in the complaint confirms that Mr. Notebaert believed that the relevant FCC rules would be "revised next year" and that it would be "*unwise* to base a business plan" on their continuation. Jon Van, *Lawmakers Seek Probe of Bells: Do Firms Agree Not To Compete?*, Chi. Trib., Dec. 19, 2002, at Business p.2 (emphasis added) (JA 44). A court assessing the sufficiency of a complaint properly considers all "documents appended to the complaint or incorporated in the complaint by reference." *Allen v. WestPoint-Pepperell, Inc.*, 945 F.2d 40, 44 (2d Cir. 1991); *see also Branch v. Tunnell*, 14 F.3d 449, 453-54 (9th Cir. 1994).

Even if the complaint could be read to allege that entry into a neighboring territory as a CLEC was the most profitable opportunity available to ILECs – which it cannot – this allegation still would not support any inference of conspiracy. As alleged in the complaint, the existing "allocation" of markets by geographic territory is not the result of any cartel agreement, but instead reflects the history of telecommunications regulation, in which each of the Bell companies was given a monopoly in its respective territory in 1982, monopolies that were largely maintained by state regulation until 1996. *See* JA 16-17, 18 (¶¶ 23, 27). Thus, no concerted action was required to establish exclusive territories.[6]

Moreover, once those exclusive territories were established, "[i]f one of the Defendants had broken ranks and commenced competition in another's territory the others would quickly have discovered that fact." JA 26 (Am. Compl. ¶ 49). Plaintiffs stated in their complaint that "[t]he likely immediacy of such discovery" makes a territorial allocation agreement "more probable." *Id.* In fact, given that territories were already established, and given the allegation that entry would provoke retaliation, the fact that secret entry would be impossible makes unlawful collusion superfluous and therefore *im*probable. *See* 6 Areeda & Hovenkamp ¶ 1425e5, at 182-83 (identical interruptions of an established

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[6] The complaint noted that "[e]laborate communications . . . would not have been necessary in order to enable Defendants to agree to allocate territories." JA 26 (Am. Compl. ¶ 48). In fact, extremely elaborate communications *were* required – litigation of a major antitrust case and negotiation of the ensuing consent decree – but those communications were entirely lawful. So, too, are communications through the various trade organizations and standards-setting bodies cited in the complaint, *see* JA 23 (Am. Compl. ¶ 46), which are an inevitable feature of an industry in which all participants are required to interconnect with one another and maintain a nationwide communications network. *See* 47 U.S.C. § 251. There is nothing suspicious about the existence of such communications. *Cf., e.g., AD/SAT, Div. of Skylight, Inc. v. Associated Press*, 181 F.3d 216, 233-34 (2d Cir. 1999) (per curiam) (rejecting a "'walking conspiracy' theory" of participation in trade associations).

course of dealing, following meetings, may support an inference of conspiracy, but a "mere failure to expand or to solicit a rival's customers" does not). As noted above, *see supra* note 4, conscious mutual forbearance, even if properly alleged, would not suffice to support an inference of agreement.

CONCLUSION

The judgment of the court of appeals should be reversed and the case remanded for reinstatement of the judgment of the district court dismissing the complaint.